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Mr. Wal. Bond

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Special Issue

Full text
of presentation
by Board Chairman
John E. Swearingen
before the New York
Society of
Security Analysts.

A review
of significant
operations
and policies of
Standard Oil Company (Indiana)

(OR PAN-AMERICAN CORP.)

Special Issue

HIGHLIGHTS

We are meeting or exceeding our corporate goals for growth and profit

Our earnings and rate-of-return continue to climb

We are penetrating more hostile environments to develop new petroleum reserves

Our chemicals operations are large, with significant potential for increasing profits

Our overseas operations are contributing to corporate profits

We are seeking opportunities to diversify into other profitable activities



Board Chairman John E. Swearingen

Volume IX • Number 2

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The terms *company*, *we*, *our*, and *its*, as used in this magazine, sometimes refer collectively to the parent company and all of its subsidiaries, sometimes to one or more of them. The shorter terms are used for convenience and simplicity.

BY WAY OF INTRODUCTION

THREE YEARS AGO, SPAN published speeches by our Chairman, John E. Swearingen, and our President, Robert C. Gunness, presented before the New York Society of Security Analysts. Response by readers to this special issue was so great that we once again publish such a presentation.

This one was made by Mr. Swearingen on April 11, 1969. In it he compares the achievements of the company since 1966 with some of the goals outlined at that time. He also covers in some detail the problems and opportunities that face our company, and the actions we have taken and plan to take in the future to profit from expanding opportunities.

The New York Society of Security Analysts is the largest single group of some 41 such societies in the United States and Canada that are part of a federation. In all, there are about 12,200 analyst members.

The object of Mr. Swearingen's talk—and of the talks our other executives make before several security-analyst groups each year—is to make our company better understood by these experts, who represent banks, brokerage houses, insurance companies, investment trusts, and other institutional investors and investment counselors. The analysts determine or recommend purchases and sales of securities by their organizations or clients. Consequently, they are keenly interested in securing information that helps them make sound judgments.

In order to present Mr. Swearingen's speech to a wide audience of stockholders, employees, annuitants, and other readers, SPAN reproduces his address in full on the following pages.

A GENERAL REVIEW

SINCE 1966, WE HAVE been proceeding toward the corporate objectives I outlined at that time, and I think the record shows substantial progress in this regard.

As I indicated then, we conceive our business—in its broad sense—to be the conservation, expansion, and the rendering of a proper return on the assets entrusted to us by our stockholders. To put it another way, we are basically in the business of making money, and we are interested in any endeavor which, in our judgment, we have the ability to handle and which holds sufficient promise of long-term profitability for our company.

In pursuit of this general objective, sometime ago we established a number of specific goals. Among these, as I stated in 1966, were:

- To improve our rate of return on net worth.
- To maintain an annual growth in earnings of 8 to 10 per cent a year.
- To increase our production of crude oil and natural gas in North America.
- To make the most of opportunities related to our present business—where we have an advantage in terms of raw materials, technology, sales contacts, or financial resources.
- To build a position in the international oil business.

These goals remain essentially unaltered, and, while we are steadily expanding our horizons, this is being done within the general framework I have outlined.

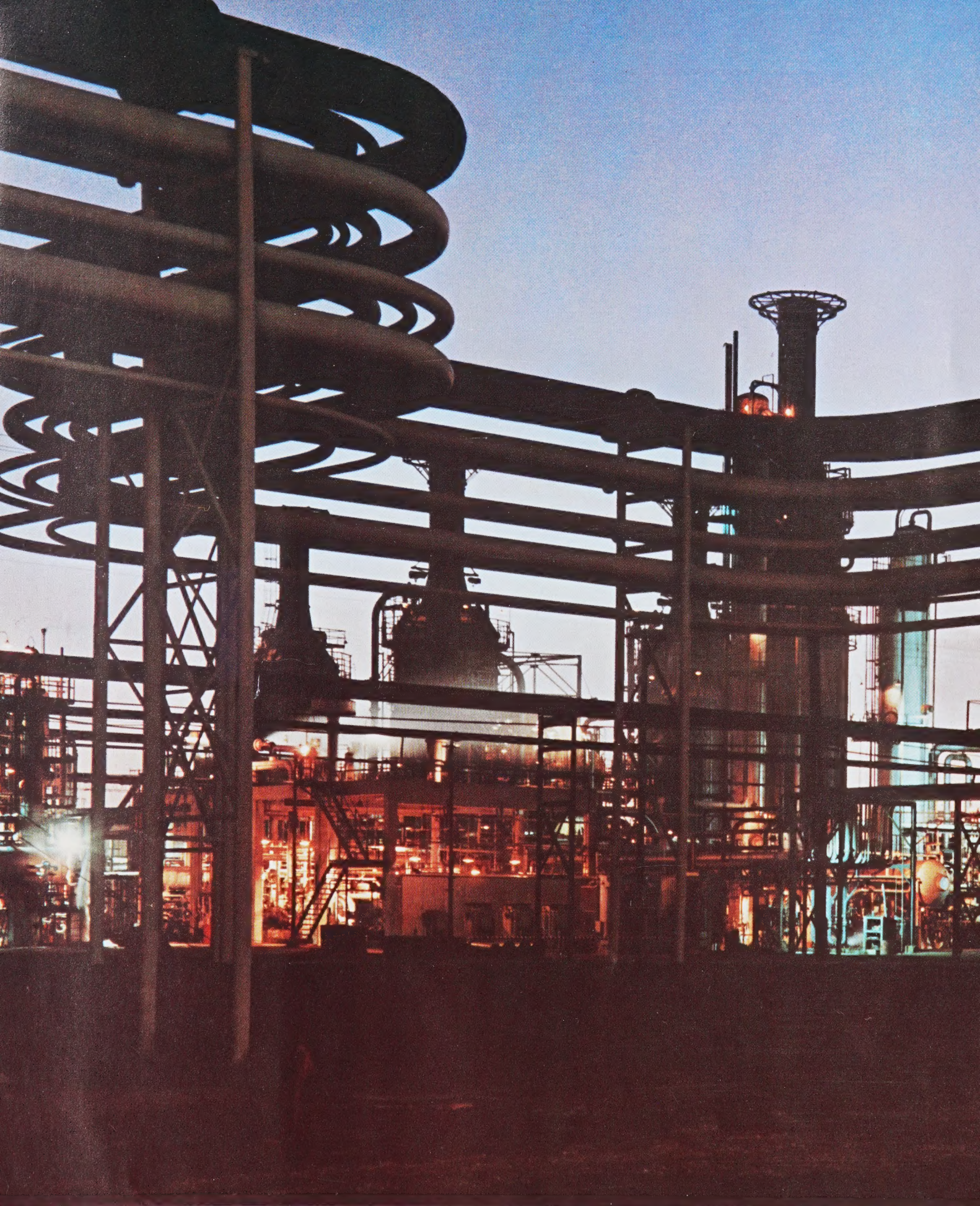
I realize it is difficult at times to identify all the companies in an industry as large as

petroleum. In our case, the difficulty is compounded by the fact that our parent company bears a Standard Oil name, while our operations are conducted through subsidiaries with different names.

Our North American exploration and production arm is Pan American Petroleum Corporation, which is the sixth-largest oil producer in the United States, and the third-largest producer of natural gas. American Oil Company conducts our domestic refining and marketing operations, in which we rank fourth in the U. S., using the brand name “Standard” in the Midwest, and the “American” and “Amoco” brands elsewhere. Amoco Chemicals Corporation is our subsidiary for the worldwide manufacture and sale of chemicals. Outside North America, our petroleum operations are conducted principally by American International Oil Company.

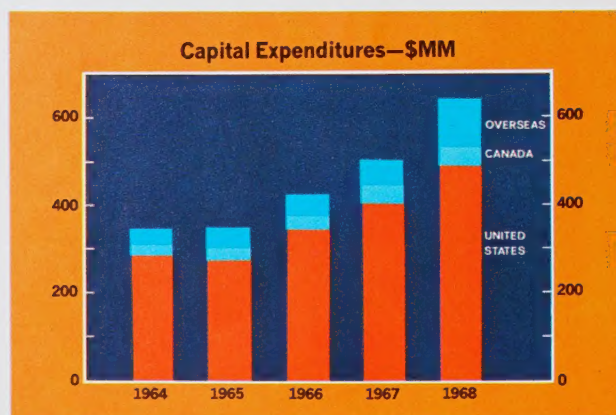
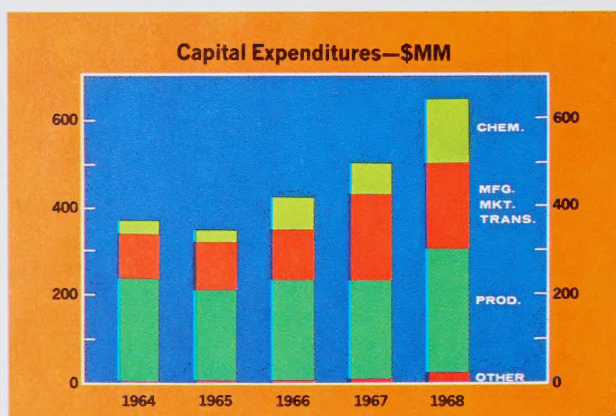
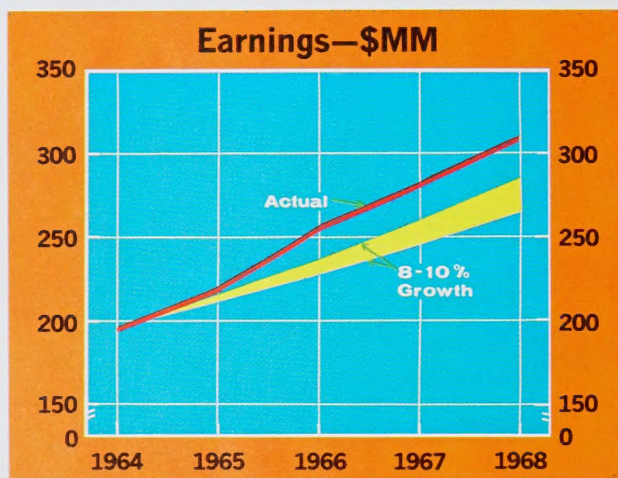
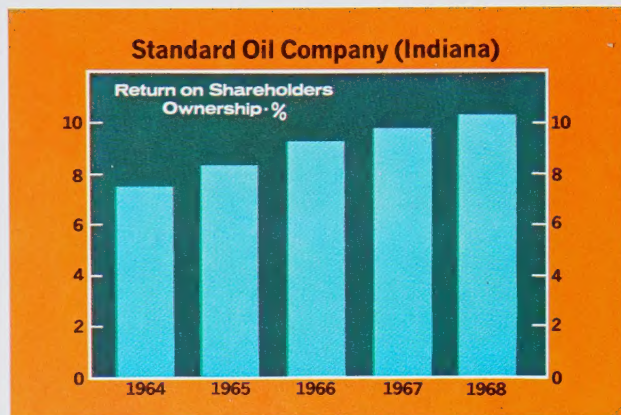
To put our total operations in focus, *Fortune* magazine’s June, 1968, listing ranked Standard Oil Company (Indiana) as the 12th largest industrial corporation in the United States in assets, 12th in net income, and 17th in sales. Among the world’s leading oil companies, we ranked 8th in assets and 7th in net income. Since that listing, our total assets have increased by \$550 million—to \$4.7 billion—and our earnings have risen by \$28 million—to \$309 million—and I wouldn’t anticipate any particular change in our relative standing when the next survey comes out.

So much by the way of background. What I would like to do now is to summarize a few measurements of recent progress toward our



Our Texas City, Tex., refinery is one of several we own where capacity has been substantially expanded.

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objectives. The first chart (at left) shows the trend in our return on shareholders' ownership over the past five years. In 1966, I stated that we considered our return on net worth—then standing at slightly over 8 per cent—to be unsatisfactory, and that we planned to bring it to 10 per cent as rapidly as possible.

This objective was reached last year, when our rate of return reached 10.3 per cent. We are working toward further improvement.

Our second objective has also been fulfilled. Over the period shown in the second chart, net earnings have increased from \$195 million in 1964, to \$309.5 million last year. The yellow area of the chart represents our target 8 to 10 per cent area for annual earnings growth. As you can see, our annual earnings growth since 1964 has averaged approximately 11 per cent.

Turning now from the consolidated financial objectives, I'd like to touch on some of the developments behind these results.

We have been carrying out a large and rapidly-accelerating capital investment program over the last five years, in all phases of our business. From a level of about \$360 million in 1964, these expenditures have risen to nearly \$650 million in 1968. The third chart reflects this increase.

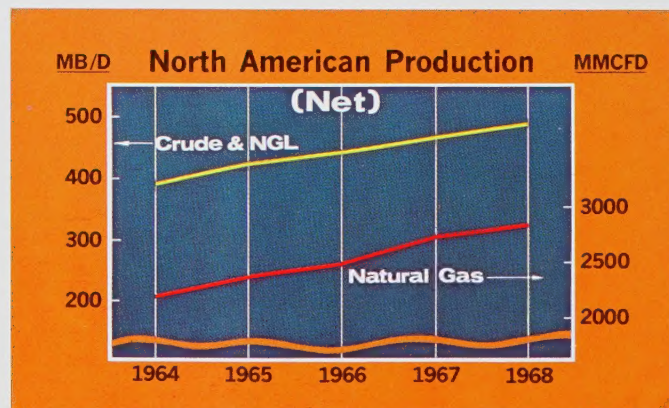
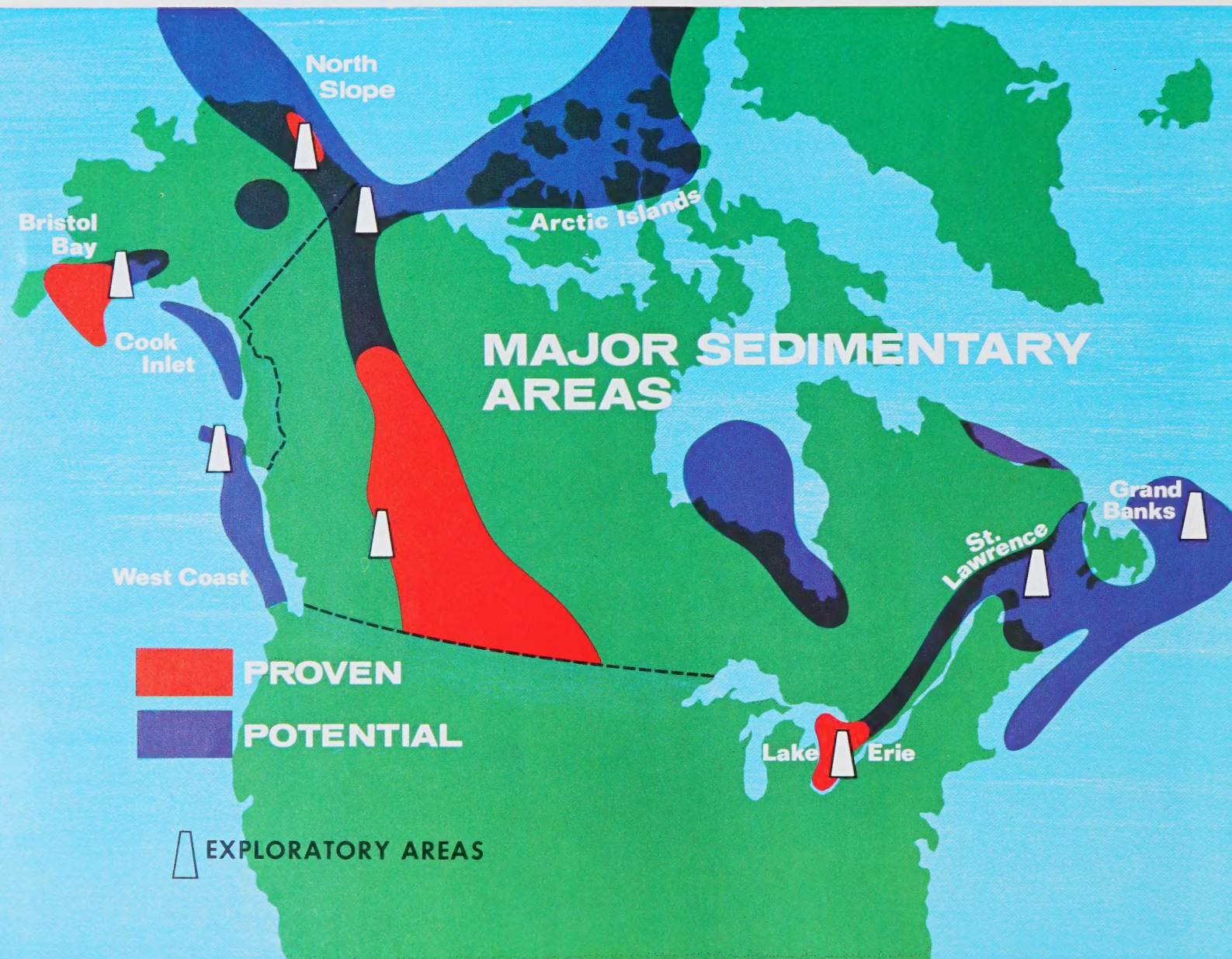
While the largest single portion of these amounts has been directed into oil and gas production, we have also been making heavy investments to modernize and enlarge our refining facilities, to upgrade and expand our marketing system, and to finance a major expansion in chemical operations.

The total capital program is broken down into expenditures for production, manufacturing, marketing and transportation, chemicals, and "other" purposes. The sharpest increase has been in chemicals—where capital spending rose to \$145 million last year. While a good portion of this reflects the cost of large acquisitions in 1968, we expect to continue a high level of chemical investments.

The fourth chart is a restatement of our capital program indicating where the investments are being made geographically. While our basic orientation is still domestic, we have been devoting considerable sums to ventures outside the U.S. Last year, \$156 million, or about one quarter of the \$648 million total, was invested in Canada and overseas.



This automated production platform is in our Vermilion Block 14 field, in the Gulf of Mexico off Louisiana.



NORTH AMERICAN OPERATIONS

NORTH AMERICAN PRODUCTION has shown gains, although not as rapid as we would like to see. As you know, this has been generally characteristic of the domestic industry in recent years. Production of crude oil and natural gas liquids has risen from an average 395,000 barrels a day in 1964 to 491,000 barrels a day last year. Natural gas production increased from 2.2 billion cubic feet daily to over 2.8 billion in 1968. (See chart, facing page.) In percentage terms, these represent production gains of 24 per cent for oil and 27 per cent for natural gas which have exceeded industry averages. We have also succeeded in adding to our net proved reserves of both crude oil and natural gas each year.

One result of declining domestic crude oil discovery rates has been an expansion of the search both seaward and northward. Since the area of greatest current interest lies to the north, we might take a moment to look at this new frontier.

The map (at left) shows the major known sedimentary areas in and around Canada, distinguishing between those with proven production and those still classified as potential on the basis of present knowledge.

The major proven petroleum province begins at the U.S. border and stretches up from western Saskatchewan through Alberta, extending into the Northwest Territories.

Although still ranked as potential in nature, this sedimentary area extends north through the Northwest Territories to the Arctic Ocean, with one branch running out through the North Slope of Alaska, and another running eastward through the Arctic Islands.

In the middle portion of the map is a large

potential province centered in Hudson Bay and covering some of the adjoining land area. To the east is a very large prospective region stretching from the Grand Banks off Newfoundland down through the waters off the Maritime Provinces, and over through the St. Lawrence area. Still other potential provinces lie in the waters off Canada's west coast.

Obviously, these areas are broadly outlined here, and include provinces with widely varying potentials.

I should like to point out that we have participated actively in the northward move. The map (see page 9) is a closer look at Western Canada, indicating the principal areas in which our company is active, and identifying the location of our major oil and gas reserves.

Our operations extend from the U.S. border through central and northern Alberta to the Beaver River-Pointed Mountain area of the Northwest Territories and the Yukon.

Our acreage holdings in the Athabasca tar sands contain an estimated total oil (tar) in place of some 13 to 14 billion barrels, and we have developed a proprietary process for recovery without using mining methods.

Returning to the frontiers (map at left) you can see that we are active, or have established acreage positions, in nearly all of the major sedimentary areas.

In the North Slope, we have held considerable acreage for some time, and participated in drilling an exploratory well there several years ago, which did not reach sands recently found productive in the Prudhoe Bay reservoir. We have an interest in some 400,000 acres on the North Slope, with our net interest approximately 280,000 acres. We are currently



Our wildcat well drills in Alaska's North Slope, some 60 miles southeast of recent Prudhoe Bay discoveries.

drilling an exploratory test at a site approximately 60 miles south of Prudhoe Bay.

In the Mackenzie Delta area to the south-east, we hold working interests varying from 25 to 100 per cent in 4.4 million acres in an area of known structural features.

Immediately to the northeast, in the Arctic Islands, we have secured permit rights from the Canadian government for about 3.7 million

acres on Banks and Prince of Wales Islands.

Off the east coast of Canada, we have established large acreage positions. With a partner, we have a 20 million acre net interest in the area of the Grand Banks. Seismic work, and a test hole and coring program, have been carried out, and plans for further exploratory drilling are proceeding.

In the Gulf of St. Lawrence, our net interest amounts to 10 million acres. We are currently evaluating results of a geophysical survey of the block. Farther to the southwest, we have been active in a drilling program in Canadian waters in Lake Erie, where we have half interest in 1.3 million acres.

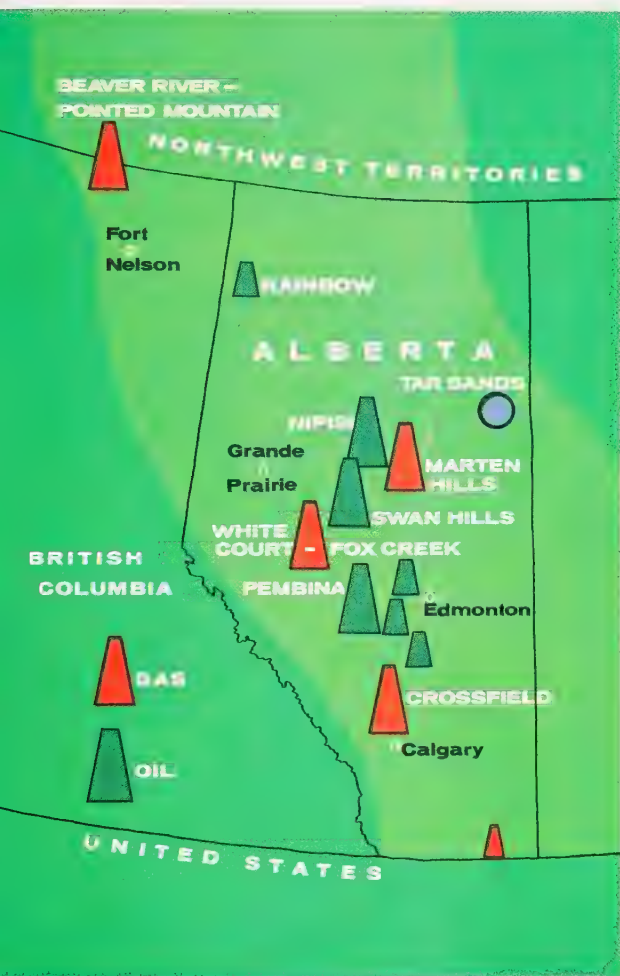
The new exploratory area indicated on the map in southern Alberta is the Ricinus-Phoenix oil and gas play northwest of Calgary. Following several promising discoveries in this area, we are currently conducting a very active exploratory and development drilling program. On Canada's west coast, we also have an acreage position, offshore British Columbia.

Finally, completing the circle, is the Cook Inlet-Bristol Bay sector of Alaska. As one of the leading operators in the Cook Inlet, we have established oil production there, as well as gas reserves. The play in Bristol Bay is more recent and we are now drilling our first exploratory well there.

I think it is clear, when you look at the map (page 6) that all of these plays are inter-related. The level of imports into the U.S. from present Canadian reserves will be affected by large discoveries in Alaska. Significant finds along the Canadian portion of the Arctic coast or in the Arctic Island area would in time alter the balance further. In light of the tremendous technological and logistics problems faced in the Far North, it will be several years before any supply from such remote areas will be a significant factor in meeting U.S. demand.

By the same token, important discoveries here, plus some demonstration of ultimate commerciability, would certainly affect the timetable for large-scale development of the Athabasca tar sands.

Moreover, major discoveries in new areas off the east coast, with better access to markets, could affect decisions for costly programs in the Arctic. Only time will determine the outcome of these frontier ventures.



CHEMICAL OPERATIONS

OUR EXPANSION into the chemical and fertilizer field—in line with the objective of capitalizing on opportunities in fields related to our basic business—has lived up to expectations, as the chart (below) indicates.

In gross terms, sales have more than trebled over the last five years—from \$110 million in 1964 to more than \$350 million in 1968. Diversification into this field is nothing new for an integrated oil company, of course. Any major oil and gas producer and oil refiner—as opposed to a straight-line chemical company—has at its disposal large quantities of the basic building blocks for chemicals and fertilizers. Such a company also has plants which routinely produce primary chemical feedstocks in great enough volume to make separation and recovery economically feasible, while providing a means for disposing of by-product fragments from chemical processes.

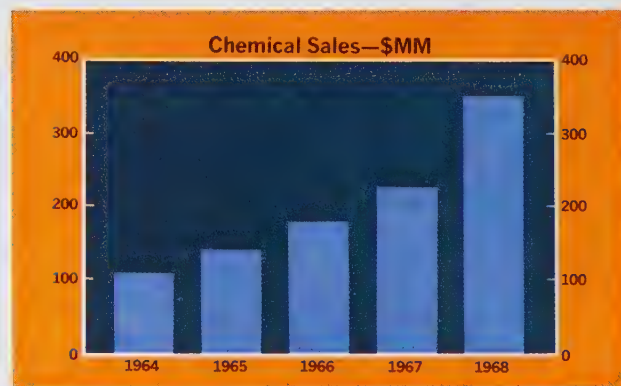
In our case, however, there have been special factors which have operated to set us apart from most of our competitors in the petroleum industry. For example, American Oil Company is the only marketer of unleaded gasoline in the United States, which we sell in the East and Southeast. Enormous quantities of aromatics, such as toluene and xylene, are needed to make any premium gasoline—and

particularly our unleaded Amoco Super-Premium. This makes toluene separation commercially more attractive for us than for others.

Large volumes of aromatics such as benzene and xylenes are also needed in chemical operations, and this dual need makes possible the design of major refinery units to meet growth demands both in petroleum and in chemicals and fertilizers.

Other differences in our approach have had to do with philosophy and strategy. We did not enter the chemical field heavily until we had built a solid commercial and technological base for long-term growth. Among other things, this approach led to emphasis on research and development, and the establishment of a strong proprietary position in basic processes—which also provides a growing source of royalty income from our licensees. Heavy emphasis on research has continued, and chemical research and development this year will account for about one third of our total research budget of nearly \$30 million.

In addition, we have given considerable attention to building marketing strengths, as an essential concurrent factor in capitalizing on our assets in raw materials and technology. An early step along these lines was to set up a technical service laboratory to work with cus-

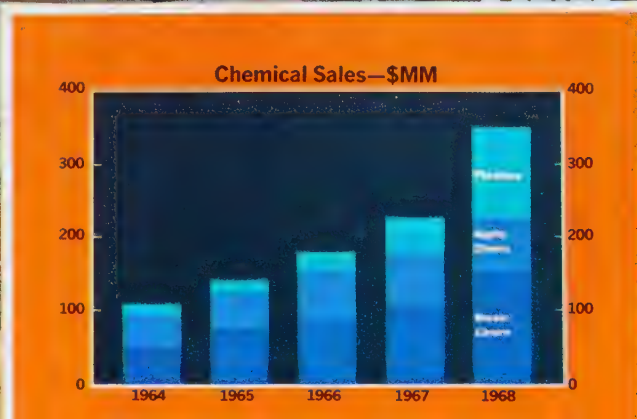




Dr. Alan Bemis conducts research at our Whiting, Ind., laboratories into the fundamental nature of how crystals form in organic chemicals.



Portion of our Joliet, Ill., chemical plant shows construction activity on recently-completed trimellitic anhydride facility. The facility has a capacity of 50 million pounds per year of the material, used primarily to insure flexibility of vinyl plastics.



tomers to determine the needs of the marketplace. Since many of our most important chemical products are designed to meet special customer needs, they would never have been developed without this market orientation.

The chart (below, left) shows chemical sales, by broad product category. These figures, incidentally, show only those sales made to arm's-length customers. The value of materials consumed internally is not included.

Our growth in plastics includes the versatile polymers which are transforming our environment at such a rapid rate. Sales of plastics have risen from only \$10 million in 1964 to over \$120 million last year. Slightly less than \$50 million of the 1968 total were sales of key plastics components to others, and over \$70 million were sales of our fabricated products.

Without attempting to go into detail on the various products involved, let me just mention a few of the current highlights. At New Castle, Del., the capacity of Amoco's polypropylene plant is being expanded from 200 million to 250 million pounds per year, and we recently announced construction of a 150 million pound per year plant in Texas, scheduled for completion by the end of next year. These facilities will give us one of the largest polypropylene production capacities in the world—some 400 million pounds per year—while the announced plans of the U.S. and foreign licensees of our process will account for another 350 million pounds annually.

Our Patchogue-Plymouth Division, a major producer of woven polypropylene for carpet backing and other industrial fabrics, has also experienced tremendous growth. Patchogue produces and sells a significant portion of the total U.S. market for carpet backing. Domestic sales in 1968 were approximately \$34 million, and are expected to reach \$48 million this year.

Future growth of this division is predicated on building additional capacity in areas with the greatest market potential. In late 1968, a new plant was opened in England, to produce approximately 20 million square yards per year of polypropylene backing, and by July of this year it will have a rated capacity of 35 million square yards. Two more foreign plants are expected to be in operation this year, and current projections call for two additional

overseas plants in 1970. Further large-scale expansion of our polystyrene, polybutene, and polyethylene capacity is also under way.

Our sales of agricultural chemicals and fertilizers have increased from about \$47 million in 1964 to nearly \$78 million in 1968. In recent years, we have broadened our operations to include liquid-mix fertilizers, which are tailored to meet specific crop and soil requirements, and we have also moved directly into retail marketing, through a network of over 700 retail outlets, along with some 310 retail LP-Gas outlets. Although the domestic fertilizer business is currently facing overcapacity and price problems, we feel this situation is temporary, and will correct itself over the next several years.

Our growth in basic chemicals shows sales rising from a level of \$53 million in 1964 to nearly \$153 million last year. These products include aromatic acids and esters, styrene monomer, paraxylene, and sulfur.

Through a proprietary oxidation process, we have built a dominant position in supplying terephthalic acid (TA) and dimethyl terephthalate (DMT)—the starting materials for polyester films and fibers. Over half of all the TA and DMT made in the world is manufactured by us or by our licensees. Major new facilities now under construction in the U.S. and in Belgium will nearly double our worldwide capacity to produce these products.

We are also the largest producer of sulfur from natural gas in the United States, and new recovery plants in Canada have almost doubled our North American production over the past year. Overseas, we are building a large half-interest sulfur recovery plant in the Persian Gulf.

Before leaving chemicals, I might note that we do not disclose profit data on the various segments of our operations. However, we have selected the product areas we have entered with a great deal of care. Despite the pressures of rapid expansion and heavy start-up costs, our chemical activities are returning a satisfactory profit, and we anticipate considerable increases in earnings from this part of our business in future years.

Now I'd like to turn to progress in building a position in the international oil business.

OVERSEAS OPERATIONS

OVERSEAS crude-oil production has shown considerable gains during the last five years, rising from about 40,000 barrels a day to over 150,000 barrels a day last year, as the chart shows (first chart, below).

This net production includes that in Argentina, which has not been reported in our

consolidated statistics since 1963, because of a contract dispute in 1962. Limited production in Argentina has continued, however, and a satisfactory settlement of differences has been reached. To give you a better measure of our production activities in Argentina during 1968, our first full year of operations under the settlement agreement, we drilled 54 new wells and production averaged 35,000 barrels a day, approaching the rate achieved prior to 1963.

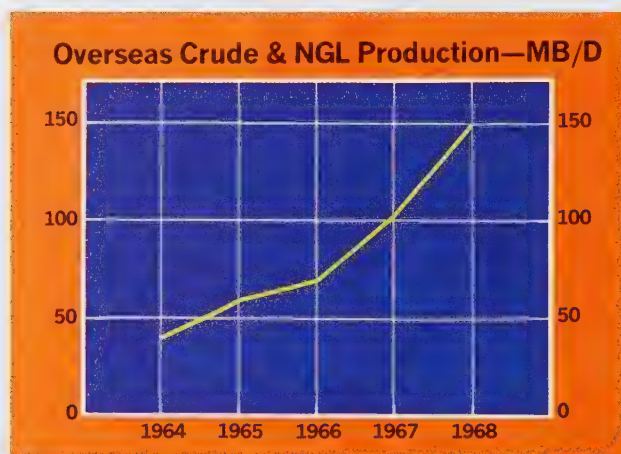
Total overseas production is, of course, considerably greater than the level shown on the chart. Gross production in 1968, including the share of our government partners, averaged over 275,000 barrels a day.

In addition to the areas of South America, North Africa, and the Middle East where we have established oil production, we have extended our overseas exploratory efforts to a number of new prospective areas—including Mauritania, Ghana, Thailand, and Taiwan.

As overseas crude oil supply sources were established, we have at the same time been creating the downstream facilities necessary to dispose of the crude.

The second chart shows growth in overseas sales of refined products and in refinery runs. As you can see, these operations have been coming into better balance each year.

From a nucleus of only 700 retail outlets in 1964, the number we now supply has increased to over 2,000—in Great Britain, West Germany, Italy, and Australia. Most of these are company-owned. Refined product sales, shown on the chart, have grown from some 24,000 barrels a day in 1964 to nearly 80,000 barrels a day last year. In terms of volume, our major





Amoco service station at Wheatheaf in England, is one of more than 2,000 operating under our brand names overseas.

foreign products in 1968 were residual fuel oil, gasoline, diesel fuels, heating oils, and LP-Gas.

Meanwhile, our foreign refinery input has increased from about 16,000 barrels a day in 1964 to about 72,000 barrels a day last year. Further expansion is projected, and we are planning a new refinery on the west coast of England. While the volumes we have been discussing are relatively small compared to the scale of our U.S. operations, I should remind you that our entire foreign structure has been created in the space of the last 10 years. More to the point is the fact that—after a decade of investing time, money, and effort in this undertaking—the overseas venture has now moved into the black. While the foreign profit contribution was modest last year, we expect con-

siderable gains from this area in the future.

Among the proven oil and gas reserves areas which show particular promise at this point are the North Sea, Egypt, and Iran.

The most important development in recent years, so far as Western Europe's energy outlook is concerned, has been the discovery of large reserves of natural gas.

We have played a leading part in this development—particularly in the waters of the North Sea. The map (at the top, right) outlines our offshore exploration licenses. Our interests in this acreage, which vary from 11 to 60 per cent, total some 2.6 million acres. The largest single portion lies in British waters, where we have a net interest totaling over 800,000 acres.

In the narrow portion of the Channel, between England and the Netherlands, are two major gas fields, which we have developed as operator for our group—which includes as our major partner the British Gas Council.

Onshore in the Netherlands are our Bergen-Groet gas reserves. Development is pending the award of a production license.

Leman and Indefatigable fields, shown in the map (at right, bottom), are among the largest discovered thus far, and our group has a major share of each. Leman field production is scheduled to begin first, and the initial pipeline to onshore terminal facilities at Bacton is now in operation after some difficulties with installation, complicated by bad weather.

Three multi-well platforms are now in place in the Leman field, where 20 successful wells have been completed, with three currently drilling. One platform has been installed in the Indefatigable field.

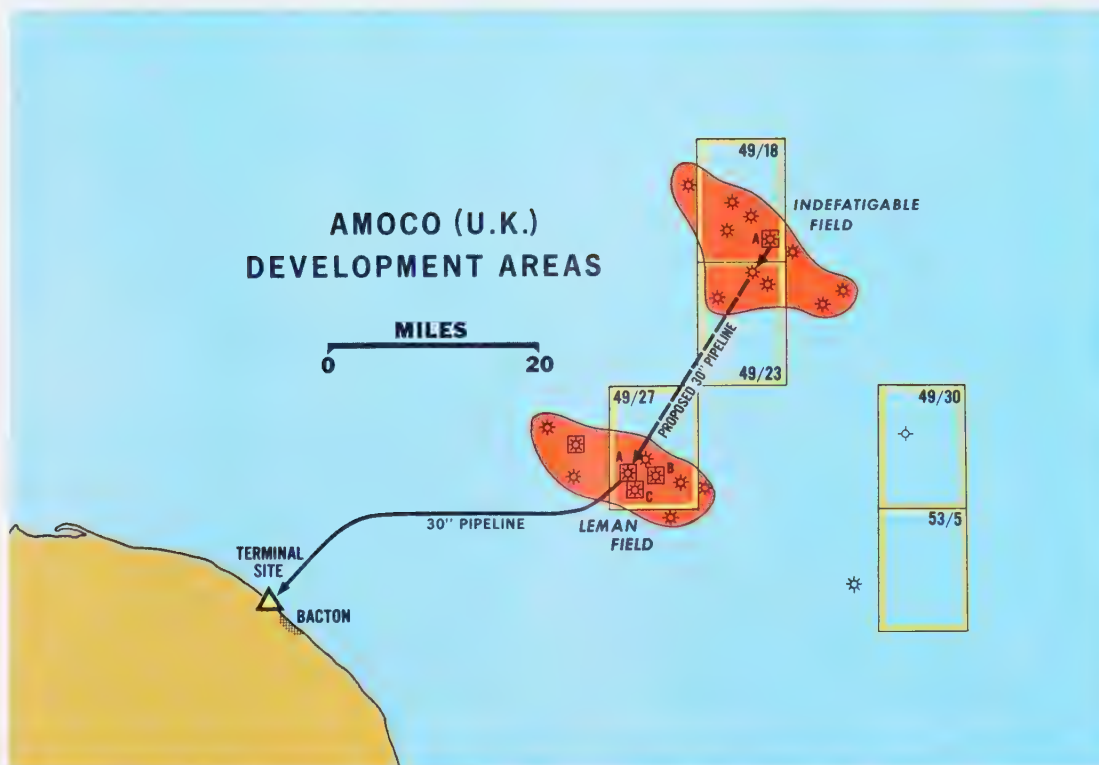
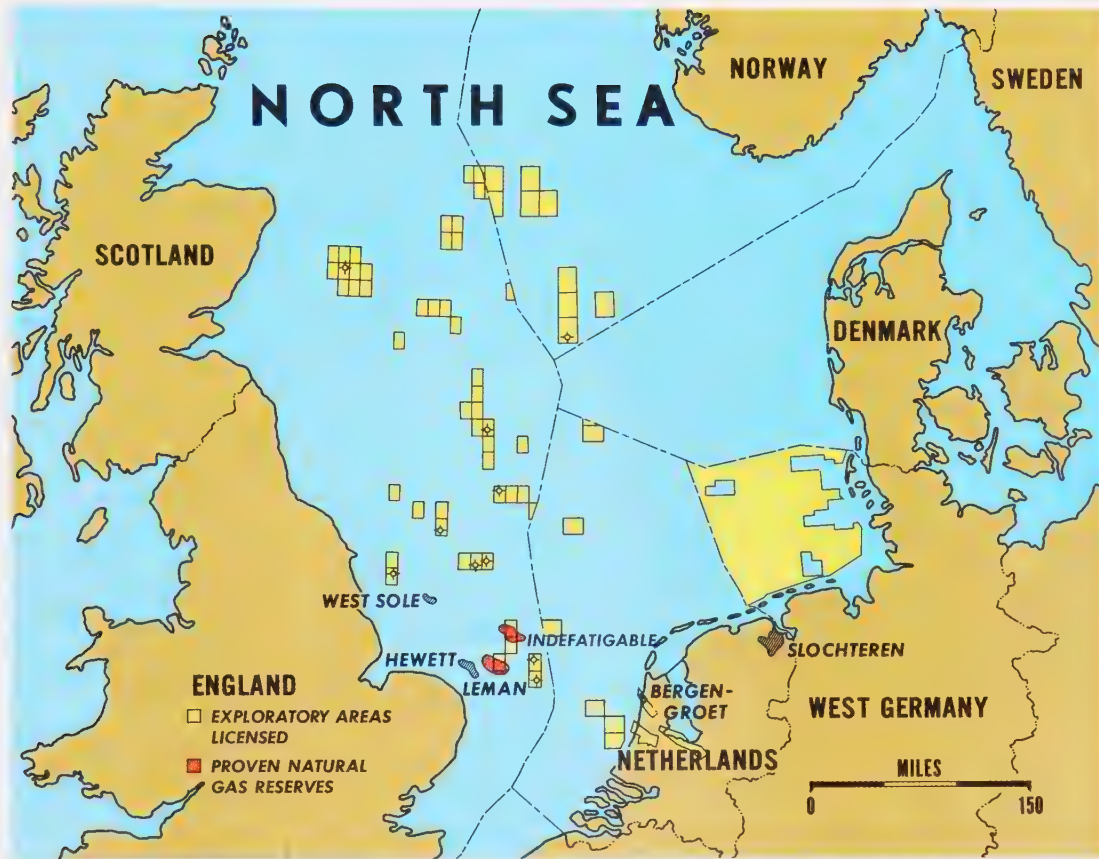
When development is completed, group production from these two fields alone will build up to about 800 million cubic feet per day—of which our share will be about 31 per cent.

Moving southeast to Africa, the map (page 18, top) shows our concession areas in Egypt. In joint ventures with the government-owned oil company, we hold two major concessions. One is onshore in the Western Desert, where we hold rights covering over 12.5 million acres. Three wells drilled in this area last year were unproductive, and a two-rig exploratory drilling program is continuing.

In the Gulf of Suez, our concession includes



Drilling and production platforms are in the Leman Bank field, in the North Sea off England's coast.





most of the offshore waters. One major oil field has already been developed—El Morgan, in the southern sector of the Gulf. Initial production began here in 1967, and we conducted an active development program last year. Thirteen new wells were drilled, and five wells drilled previously were tied into production facilities. At year-end, a total of 33 wells had been drilled, of which 26 were connected to producing facilities. Production has climbed rapidly, and a new daily record of 194,000 barrels was reached early this year, of which approximately 78,000 barrels was net to us. Additional facilities, enabling an increase in total field production to 300,000 barrels a day, are planned. While continued closure of the Suez Canal increases transportation costs, we are making regular shipments to our own overseas refineries and to third parties, with the balance going to our government partner.

The map (lower left) shows our contract areas in the Persian Gulf, off Iran. Our initial discovery was the Darius field, followed by the Cyrus field. The latest is the Fereidoon field, south of Cyrus.

Fereidoon development has been delayed because of a boundary dispute between Iran and Saudi Arabia, whose territorial waters lie to the west of our concessions. Late last year, however, the two governments reached agreement on the boundary line indicated on the map, enabling us to proceed with field delineation and with working out plans for development with our partner. In the initial phase of development, production is planned at a level of 100,000 barrels a day gross, with a further expansion beyond that in prospect.

Gross production from Darius reached an average of over 93,000 barrels a day in 1968, with 10 wells currently on production. Completion of another well and additional facilities is expected to lift total production to 122,000 barrels a day shortly. Cyrus production averaged about 8,800 barrels a day gross during the year, and we hope to step up production substantially in 1969, as markets for this particular type of heavy crude can be developed.

That completes our progress report on operations. While necessarily brief, I trust it is sufficient to give you some measure of our current direction.

A LOOK AT THE FUTURE

FROM THE SCALE of recent developments, particularly in chemicals and in foreign operations, I think you can appreciate that this has been a period when we have absorbed some very large costs. This has been accomplished while meeting our targets for improved earnings, and I would expect this pattern to extend into the future. Since our goal is long-term growth, further heavy expenditures can be anticipated in the years ahead.

As part of our long-range planning, we have been appraising new ventures outside the oil and chemical business. Late last year we announced plans for merger with Cerro Corporation, in order to enter the mining business. However, further action on this proposal has been deferred to permit additional evaluation of political developments in Peru.* With our chemical business firmly established, and with foreign operations in the profit column, we are now in position to consider moving into new areas that will complement our current business, and I have no doubt that action in this direction will be forthcoming.

In regard to the short-term outlook, we have recently experienced a combination of wage and price increases which have had offsetting effects on company profit. While it is not possible to say how long or at what level the increases in crude and product prices will be in effect, there is no doubt as to the wage increases negotiated this year.

Most of the gain from higher product realizations is offset by increased labor costs, while higher costs for purchased crude largely cancel out the benefits on the other side of the scale. In terms of aftertax income, the combined effect of these counterbalancing factors leaves us about where we were before the changes.

In any event, we expect to meet our objectives again in 1969. Earnings have increased each year in the last decade, with per-share earnings showing a 10 per cent compound rate of growth for the last 10 years and 11 per cent for the last five. In 1969, we look forward to another record year.

Long-term growth in profitability remains a central goal, and I think the major restructuring which has taken place in recent years—particularly in our chemical and foreign operations—has put us in excellent position to capitalize on future opportunities.

* Merger plans were abandoned in May by mutual agreement of our Company and Cerro Corporation.

QUESTIONS AND ANSWERS

FOLLOWING the presentation by Mr. Swearingen, there was a question-and-answer period, which is reproduced in part on this page. Both questions and answers were edited to avoid duplication and in the interests of brevity and clarity.

QUESTION: I wonder if you could comment on the Cook Inlet prospects?

Answer: All the fields in Alaska's Cook Inlet have been somewhat of a disappointment in that the producing sands have turned out to be tight, and we and a number of the other operators are currently installing water flood facilities to sustain production. I would hope that we can maintain our production and perhaps increase it in 1969 over 1968.

Question: How do you size up the current political difficulties in the Middle East?

Answer: Maybe I can summarize the situation in one word by saying it's confused. It seems perfectly obvious from even a casual reading of the newspapers that guerrilla activity between the Arab states and Israel has intensified in recent months. My own feeling is one of apprehension that this will burst into something more serious than shooting across the Canal unless some settlement of a more or less permanent nature is brought about within the next few months.

Barring some major resumption of hostilities, we wouldn't expect our program to be affected. Just to be sure you understand, the refineries at Suez which were shelled by the Israelis belong to the Egyptian government and not to us.

Question: I have a question on capital structure. Your percentage of debt to total capital has roughly doubled in the past five years, and of course currently is in line with the industry as a whole. In view of your tremendous capital requirements, do you expect a continuing increase in this percentage, or do you feel that internal cash generation can be sufficient?

Answer (by L. Chester May, Vice President Finance): We anticipate that we will need funds in addition to our internal generation over the next several years. We will probably get some substantial part of it through debt. I don't anticipate that we're going to have any problem in the foreseeable future in obtaining the capital that we need.

Question: Most oil companies have been rather disappointed in chemicals growth. Could you be more specific in regard to your chemicals profits?

Answer: As I said in my prepared remarks, we don't disclose the rate of return on parts of our business. Our chemical operations are

making a satisfactory profit even in the light of the heavy start-up costs of recent years.

We have carefully selected the areas into which we have gone. As you know, plastics and polyester fibers are growing very rapidly indeed. We think we have a dominant position in the manufacture of the basic raw materials for polyester fiber, and certainly a very strong position in polypropylene. Our philosophy has been that a proprietary position will give us a higher profit margin than run-of-the-mine materials that are available to everybody else.

Question: What is the outlook for fertilizer prices?

Answer: Right now it's dim. However, we think the long-term prospects for fertilizer in this country are good, although it may take several years for the industry to get out of the woods on the supply-demand relationship.

Question: How about sulfur?

Answer: As you know, the price has taken quite a tumble. But I would say for the world as a whole—looking ahead eight to ten years—the problem is going to be a shortage of sulfur, not a surplus.

Question: I think it's timely to ask if you would comment on the outlook for changes in the import program.

Answer: I think the key question as far as the oil industry is concerned is the entire foundation of the program, whether control of oil imports into the United States is essential to national security or whether it isn't. If it is, you go down one road. If it's not, you go down another.

Personally, I believe strongly that domestic oil is essential to the national security of this country, and I think we've had two demonstrations in the last ten years when there were interruptions in supply from the Middle East.

I hope that the cabinet committee appointed by the President will report out recommendations which will eliminate many of the inequities in the present program. I hope you are familiar with most of them. I won't take time to go into them now, but I do not believe the import control program should be used to favor one company over another, or to accomplish special social objectives, whether they be in Puerto Rico, Maine, Appalachia, Georgia, or somewhere else.



STANDARD OIL COMPANY

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SHAREHOLDER NEWS

a quarterly report from

STANDARD OIL COMPANY
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Regular Dividend

Standard Oil Company (Indiana) is paying a regular quarterly cash dividend of 57½ cents a share on June 10, 1969, to shareholders of record on May 8, 1969. This is the Company's 293rd dividend. Quarterly dividends have been paid regularly for 57 consecutive years.

First Quarter 1969 Earnings

First quarter earnings in 1969 were the highest for any single quarter in the Company's history, shareholders were told at the annual meeting, held May 1 at the Whiting, Indiana, Community Center.

Chairman John E. Swearingen reported consolidated net earnings of \$94,000,000, or \$1.33 per share for the quarter, an increase of 9.5 per cent over the \$85,900,000, or \$1.21 per share, earned in the 1968 period.

Total revenues increased 7 per cent, to more than \$1 billion. Mr. Swearingen said the Company expects another record year in 1969 in both operations and earnings.

Net production of crude oil and natural gas liquids, natural gas sales, refinery runs, and sales of refined and chemical products all showed gains from the previous year's first quarter.

Action by Shareholders

More than 84 per cent of the total outstanding shares of the Company were represented at the meeting either in person or by proxy. We thank the thousands of stockholders who provided this tangible evidence of their constructive interest in the Company's affairs.

Shareholders reelected 16 members of the board of directors.

Comments by Chairman Swearingen and President Robert C. Gunness follow.

COMMENTS BY MR. SWEARINGEN

As you are aware from the Annual Report, our Company again met its major objectives in 1968, including continued growth in earnings, improvement in the rate of return on shareholders' investment, and expansion of our operations.

Net earnings totaled \$309.5 million, or \$4.37 per share versus \$3.97 per share in 1967. Dividends were also increased, to \$2.10 per share compared with \$1.90 paid in 1967, and 1968 marked our tenth consecutive annual increase in both earnings and dividends. Rate of return on shareholders' investment reached 10.3 per cent.

Further gains have been made in the opening months of 1969, and first quarter earnings of \$94 million were the highest for any single quarter in our corporate history, advancing 9.5 per cent above the \$85.9 million earned in the comparable 1968 period. Earnings per share for the quarter reached \$1.33, versus \$1.21 a year ago. Total revenues increased 7 per cent, to more than \$1 billion.

Record Operations

Net production of crude oil and natural gas liquids advanced 2 per cent above last year's first quarter level, to an average of 609,000 barrels per day, while refinery input averaged 962,000 barrels daily, a gain of 7 per cent. Refined product sales increased over 6 per cent, and averaged over one million barrels a day.

Sales of natural gas were 17 per cent above the level set in 1968, and averaged

close to 3.4 billion cubic feet per day. Sales of chemical products registered a gain of nearly 8 per cent for the three-month period, to a total of \$86 million.

So far as the short-term outlook is concerned, we have recently experienced a combination of wage and price increases which have had offsetting effects on Company profit. While it is not possible to say how long or at what level the increases in crude and product prices will be in effect, there is no doubt as to the wage increases negotiated this year. In terms of after-tax income, the combined effect of increased labor costs, higher product realizations, and advanced crude prices leaves us about where we were before the changes.

In any event, we expect to meet our objectives again in 1969, and look forward to another record year in both operations and earnings.

Tax Reform

Now I would like to comment on a subject which affects all of us—namely tax reform. The Tax Foundation has recently informed us that Americans will work over 2½ hours of each eight-hour day this year to earn the money needed to pay combined federal, state, and local tax bills. Moreover, I think we must be resigned to the fact that taxes are going to continue to rise, in order to provide the funds needed to improve the quality of life at home and to meet our responsibilities abroad.

Each of us is already concerned about the present level of taxation, since taxes reach increasingly into every aspect of our lives, from the cradle to the grave. At the moment, the focus of public concern has to do with inequities in the tax structure, and the Congress is undertaking what

many hope will be a major reform of the federal tax system.

The least we can expect is that the system can be made more comprehensible, more equitable, and better designed to serve the national interest than the present haphazard jungle of rules and requirements which has grown up over the last 56 years.

One aspect of the code which is receiving considerable attention is the tax treatment of petroleum operations — particularly oil and gas production. Since we rely on oil and natural gas for nearly three-fourths of the energy needed to run our economy, this is a subject of legitimate and proper concern to every citizen. The first requirement of an industrial nation is an uninterrupted supply of low-cost energy. A tax structure designed to encourage and maintain this supply is essential.

The spectacular performance of the U.S. economy is evidence that this objective has been met. In regard to costs, even with the recent and long overdue increase in prices, gasoline prices—excluding steadily rising excise taxes—are little more than one cent a gallon above the level of 12 years ago, while domestic crude prices are still about where they stood in 1957. By any measure, petroleum prices stand out as one of the most stable elements in an inflationary economy.

However, our concern here is with tax equity, and critics charge that the petroleum industry is the beneficiary of unequal treatment which allows it to escape paying its fair share of taxes—principally because of the percentage depletion deduction which has been part of the tax code since 1926.

As shareholders in our Company, I think it is important that you recognize a

serious fallacy in this argument. It rests entirely on a comparison of the federal income tax burden on the petroleum industry with that of other industries. Because of the vital importance of oil and gas to our economy, and because of the distinctive combination of high risk and tremendous capital requirements found in our industry, differential income tax treatment has been established for petroleum operations as a matter of public policy to encourage the discovery of oil and gas.

At the same time, no rational conclusions as to the equity of a taxing system can be reached on the basis of a single type of tax—a point repeatedly made by tax scholars. Decisions of tax policy should take into account the whole range of tax burdens on any given industry, and—unlike other industries—the petroleum industry's tax payments to state and local governments are considerably greater than its federal income tax payments.

As a result, the oil industry's total domestic direct tax burden is around \$2.5 billion annually—or over 5 per cent of gross revenues—which is on a par with other manufacturing industries. In addition to this are the indirect excise taxes on petroleum products, which total over \$8 billion a year. All told, the petroleum industry and its operations comprise one of the largest sources of tax revenues to be found in the entire economy.

Profit Record Reviewed

The clearest demonstration that the oil industry is not the beneficiary of some hidden tax advantage lies in its profit record. Over the 20-year period through 1966, the earnings of U.S. oil companies averaged 12.5 per cent of invested capital, versus

12.7 per cent for all manufacturing companies. In 1967, earnings of the oil companies represented among *Fortune Magazine's* listing of the 500 largest U.S. industrial corporations averaged 11.2 per cent of invested capital, again less than the 11.3 per cent record for all industry.

I think all of our stockholders are aware of the strenuous efforts it has taken to

Standard Oil Company <Indic
Consolidated Sta

Revenues:

Sales and other operating revenues (including excise taxes)	
Dividends, interest, and other income	
Total revenues	

Costs, Expenses, and Taxes:

Purchased crude oil, petroleum products, merchandise, and operating expenses . .	
Exploration expenses, including dry hole costs	
Selling and administrative expenses	
Taxes ¹	
Depreciation, depletion, amortization, retirements, and abandonments	
Interest expense	
Income applicable to minority interest . . .	
Total costs, expenses, and taxes	

Net Earnings

Net Earnings Per Share

¹ Includes taxes on income amounting to \$
1968, after reflecting deferred taxes of

bring our rate of return up to last year's level of slightly over 10 per cent. Nor do we consider our tax burden to be light in any sense. The \$103 million which we paid in property, severance, production, and other taxes, added to some \$93 million in federal and other taxes on income, gave us a total direct tax bill of \$196 million. Direct taxes amounted to six cents on

> and Subsidiary Companies ent of Earnings

<i>First Three Months</i>	
<i>1969</i>	<i>1968</i>
\$1,041,375,000	\$ 982,839,000
30,079,000	18,771,000
<u>1,071,454,000</u>	<u>1,001,610,000</u>
494,296,000	461,356,000
34,716,000	38,379,000
136,092,000	132,533,000
231,117,000	212,078,000
66,832,000	60,019,000
12,266,000	9,682,000
2,089,000	1,707,000
<u>977,408,000</u>	<u>915,754,000</u>
<u>\$ 94,046,000</u>	<u>\$ 85,856,000</u>
<u>\$1.33</u>	<u>\$1.21</u>

422,000 for 1969 and \$27,431,000 for 1968, respectively. \$23,000 and \$4,550,000, respectively.

every dollar of sales, and were considerably greater than the dividends paid to our shareholders. In addition to these direct levies, state and federal excise taxes paid on our products totaled over \$704 million.

Any increase in this already high level of taxation would have adverse effects on future earnings and dividends, and on our ability to generate the capital required to continue the search for new reserves of oil and natural gas. Our combined exploration expenditures and capital expenditures for production in 1968 totaled \$434 million.

These are all considerations of which you should be aware, and which need to be taken into account by your representatives in Congress as the study of our tax system progresses. It may well be that applications of the present code have undesirable effects in individual instances, and some reforms may be in order. But the claim that the petroleum industry as a whole is not paying its fair share of taxes is false.

If there are any hidden benefits in the petroleum tax structure, it is clear that competitive forces have seen to it that they have been passed on to the public. It is equally clear that any significant increases in the petroleum tax burden will simply add to the cost of energy for all consumers, including the government itself.

COMMENTS BY MR. GUNNIES

Exploration and Production

As a result of generally declining discovery rates within the United States in recent years, and with demand for oil and gas rising steadily, North American exploratory interest has shifted to a series of frontier areas in Canada, and in the Alaskan and Canadian Arctic.

Our Company has been conducting an active program on these new frontiers, as you know, and further progress has been made since the start of the year.

In Alaska, our net holdings now total approximately 870,000 acres, including some 280,000 acres on the North Slope, where a 50 per cent interest wildcat recently tested gas at flow rates up to 12.5 million cubic feet per day, at about 4,300 feet. This well is preparing to drill ahead to the objective depth of 10,000 feet. A second important exploratory well is currently drilling in the Bristol Bay area, to the south.

Offshore northern Alaska, in the Beaufort Sea, we will be the operator of a group seismic survey covering some 1,800 square miles of the Arctic Ocean, scheduled for July and August of this year.

In the Canadian Arctic, we recently acquired over one million acres of exploratory permits on and around Prince of Wales Island — approximately 500 miles east of the 2.5 million-acre block previously acquired on Banks Island.

In the Beaver River-Pointed Mountain area of northwest Canada, where we have discovered major natural gas reserves, several more successful development wells have been completed, the most recent of which tested up to 40 million cubic feet per day from a single pay interval. Gas from this area will begin moving to market next year.

In the Ricinus-Phoenix area of southern Alberta, where we are conducting an active exploratory and development drilling program, we have confirmed the presence of substantial oil and gas reserves, and purchased a 60 per cent interest in a 12,800-acre drilling reservation in early March, plus additional acreage in April.

Meanwhile, work is under way on construction of a semi-submersible drilling unit for exploratory drilling off Canada's east coast, where we have large acreage holdings on the Grand Banks and the Flemish Cap. The new unit, designed to drill to 25,000 feet in water depths up to 800 feet, is scheduled to be in operation by mid-1970.

Gains Overseas

Significant gains have also been made in our overseas exploration and production programs this year. In the North Sea, we have completed six additional successful gas wells in our portion of the Leman and Indefatigable fields. After some installation difficulties, compounded by bad weather, the pipeline to shore from the Leman field is now in operation, and commercial deliveries have begun. Gas is currently moving to market at a rate of 130 million cubic feet per day, with deliveries expected to rise to over 300 million cubic feet per day later this year. Our share of this production is approximately 30 per cent.

In the El Morgan oil field in the Gulf of Suez, we have completed four new development wells since the start of the year, and gross production in March averaged 185,000 barrels per day, of which approximately 74,000 barrels a day was net to us. Additional facilities, to enable an increase in total field production to 300,000 barrels a day, are planned.

In the Persian Gulf, we are proceeding with delineation of our latest new field discovery—the Fereidoon field—and are working out plans for development with our government partner. Initial production of this field is planned at a level of 100,000 barrels a day. Our share would be approxi-

mately one-half of this volume.

Offshore Trinidad, drilling is continuing, to delineate the potentially significant new natural gas area, where three out of five exploratory wells tested gas last year.

As indicated in the Annual Report, we have extended our overseas exploratory efforts to a number of new prospective areas, including Mauritania, Thailand, and Taiwan. The most recent addition to this list is the Republic of Ghana, where we and two other U.S. companies have been granted an exploration concession covering about 1,600 square miles in the Gulf of Guinea. Seismic operations here will begin as soon as possible.

Marketing

First-quarter gains in refined product sales were encouraging, particularly since we are measuring them against a period of very strong demand in the early months of 1968, when abnormally cold weather stimulated extremely high consumption.

While more normal weather prevailed this year, our domestic sales nevertheless advanced nearly 4 per cent above the 1968 level, averaging over 990,000 barrels per day. This gain was achieved despite work stoppages at our refineries beginning in January and extending through early March.

Expansion of our overseas marketing operations also continued on schedule, and foreign sales of refined products rose to 100,000 barrels a day, from a level of slightly over 70,000 barrels a day in the first quarter of 1968. Our overseas marketing network was also increased, and the number of retail outlets supplied now stands at 2,088, versus 1,654 at this time last year.

Chemicals

Both here and abroad, our chemical operations continue to grow rapidly. At New Castle, Delaware, our polypropylene capacity is being expanded from 200 to 250 million pounds per year. Meanwhile, we have announced construction of a new polypropylene resin plant at Chocolate Bayou, Texas, with a rated capacity of 150 million pounds per year—expected to go on stream at the end of next year. Together, these facilities will place us among the world's largest producers of this versatile plastic, which is used in textile fibers, films, and molded products.

At Decatur, Alabama, construction of new facilities to produce an additional 400 million pounds a year of purified terephthalic acid will begin shortly. This product is used to make polyester fiber for automobile tire cord, permanent press and drip dry materials, and films for electronic recording tape.

Our sales of woven polyolefin fabric, used chiefly for carpet backing, have also been undergoing accelerating growth. With current domestic production running at a rate of 250 million square yards per year, we now supply a considerable portion of the total U.S. market for carpet backing, and expansion to a capacity of 350 million square yards by the end of this year has been approved.

Markets for this product are also being developed overseas. Late last year, a new plant was opened in England, to produce approximately 20 million square yards of backing per year, and by July of this year the location will have a rated capacity of 35 million square yards. Two more foreign plants are expected to be in operation this year, and current projections call for two

additional facilities outside the United States in 1970.

In Belgium, our new terephthalic acid plant is nearing startup operations, as are the sulfur and liquefied petroleum gas facilities on Kharg Island, in the Persian Gulf.

New Research and Office Facilities

Here in the United States, we have continued with plans to expand research and office facilities to meet the demands of our growing operations.

The first contingent of scientific personnel has moved into the new Naperville Technical Center, in suburban Chicago, where the first structure will house our technical service and plastics laboratory staffs for chemicals. The second major building, a new chemical research laboratory, is expected to be ready for occupancy by mid-1970. When completed, this center will more than double our facilities for research in chemicals, and in petroleum products and processing.

In March, we also named the architects for our new headquarters building in downtown Chicago, near the lakefront. This will be one of the largest office buildings in the city, and will be international headquarters for the parent company and our Chicago-based subsidiaries. The construction schedule calls for partial occupancy of the structure by the end of 1972.

As you have been informed, we again expect to improve our record in 1969. On behalf of the 48,000 people who make up our Company, I would like to thank all of our shareholders for their continued support in our common effort.

Cerro Merger Abandoned

Standard Oil Company (Indiana) and Cerro Corporation have abandoned plans for the merger of the two companies initially announced in November, 1968.

John E. Swearingen, Standard's chairman, and Robert P. Koenig, Cerro's president, stated on May 14, 1969, that a number of developments since the initial announcement led to the decision to terminate further merger efforts.

STANDARD OIL COMPANY
<INDIANA>
910 SOUTH MICHIGAN AVENUE
CHICAGO, ILLINOIS 60680